

VOTE 32. - DEPARTMENT OF PUBLIC ENTERPRISE

33. The transfer of the public telecommunications system from State control to the Private Sector

Background

Control over public telecommunications, since its advent in Ireland in 1869, had, up to 1983, been vested solely in the predecessors, in title, of the Minister for Public Enterprise. Direct departmental management of the system ceased in December 1983 when the Government set up a company, Telecom Éireann Ltd, to manage and administer the public telecommunications system. The Minister for Public Enterprise retained responsibility for determining and executing policy on behalf of the Government in relation to telecommunications and was also responsible for exercising a general supervisory role over the activities of the company. The shares in the company were vested in the Minister for Finance and the Minister for Public Enterprise (The Ministers).

In December 1996, the company was re-registered as a public limited company, Bord Telecom Éireann plc (BTE). BTE was the parent company of a group of companies which provide a range of telecommunications services. In September 1999 the Company changed its corporate identity to Eircom plc.

The formation of the public limited company was the first step in a series designed to allow for the possibility of the State divesting itself of its share holding in the company and effectively ending State control of the telecommunications system.

Strategic Alliance

In December 1996, BTE entered into a strategic alliance with Comsource, an entity owned by KPN Telecom BV of The Netherlands (60%) and Telia AB of Sweden (40%). The purpose of the strategic alliance was to strengthen BTE in advance of the loss of its monopoly position in the Irish telecommunications market which would arise following the liberalisation of the telecommunications sector in the EU.

A complex set of arrangements were put in place for the strategic alliance under which Comsource was to acquire 20% of BTE with an option, exercisable before December 1999, to acquire a further 15% of the company. The agreement provided that Comsource would pay £183m for its initial 20% and £200m for a further 15% in the event of it exercising its option. The strategic alliance agreement also contained a clawback provision, which provided that Comsource would pay an additional amount for the shares it purchased, which broadly equated to 60% of the increase in the real value of the shares in the three years following the agreement, when account was taken of the normal rate of return which KPN and Telia would earn on their capital. Immediately prior to the public offer of the shares in July 1999, Comsource exercised its option to acquire the additional 15% share holding and, in January 2000, paid an additional £1,138m under the clawback provision.

Under the terms of the strategic alliance agreement the State agreed to provide funding of £220m to the company from the proceeds of the sale of the shares to Comsource.

The terms of the agreement were effected as follows:

- Ministers sold and Comsource purchased 15,869,887 shares for £33m.
- BTE issued and Comsource purchased 72,443,181 shares for £150m.
- BTE issued and the State acquired 33,806,818 shares for an interest bearing Promissory Note of £70m. (This was paid in December 1998. Interest of £9m was paid on the Note)
- State gave Comsource an option exercisable within three years to buy 66,234,800 shares for £200m.

Under the Strategic Alliance the Government also enacted legislation to provide for the continuation of the class D modified PRSI rates to be applied to the company for all employees who commenced their employment in the company prior to 5 April 1995.

Employee Shares

As part of the framework for the part or complete privatisation of the company, the Government and the unions operating in BTE agreed, in February 1997, to the establishment of an Employee Share Ownership Plan (ESOP) which provided for 14.9% of the shares being transferred to the employees. A trust was set up to facilitate the transfer of the shares to staff - Employee Share Ownership Trust (ESOT). The transfers were to be effected as follows:

- 5% of the shares to be transferred in stages based on implementation of agreed productivity measures and changes in work practices. Two thirds of these shares were transferred to ESOT in May 1999. The remaining one third were transferred in May 2000. It is intended that the shares will be distributed to staff not later than May 2004 subject to prevailing taxation conditions.
- 9.9% to be purchased for an agreed price of £190m which was payable to the Exchequer as follows:
£100m paid by BTE in May 1999, in return for which staff agreed to make contributions to their pension scheme and waived rights to certain bonus arrangements.
£60m and £30m funded by borrowings by ESOT, were paid in May 1999 and July 2000 respectively.

Initial Public Offering

In March 1998, the Government decided that an Initial Public Offering (IPO) of the shares would take place in 1999. Initially, it had been decided that the remaining shares held by the Ministers would be offered for public subscription in a number of tranches. However, following assessment of the reaction by institutional investors and the number of individuals who, following a registration process, indicated an interest in acquiring shares in the company, it was decided to issue 48.9% of the total company shares in a single tranche under the IPO.

The remaining 1.2% of the company's shares were retained by the Ministers for distribution as a loyalty bonus, on the basis of one share for every 25 shares held, to retail investors who held their shares for a period of one year after the date of the IPO.

The final decision on the extent of the stake to be offered at the IPO was made by a Cabinet Sub-Committee and was determined by factors such as maximising the return to the Exchequer, having a wide share ownership and value for money on expenditure related to the sale.

The Government appointed joint advisers and global co-ordinators to advise in relation to the strategic and financial aspects of the execution of the flotation, to co-ordinate the offering and to ensure that the flotation was successful and that there would be investor confidence in the shares. They also gave advice as to the price at which the shares should be issued taking account of all of the factors and interests involved and on compliance with legal and International Stock Market requirements. They were selected on the basis of a competitive tendering process and their fees amounted to 1.7% of gross sales revenue.

The following legislative changes were also effected:

- The Postal and Telecommunications Services (Amendment) Act, 1999 was introduced to enable the State to lower its share holding to below 50%.
- The Companies (Amendment) (No.2) Act, 1999 was also introduced to enable price stabilisation in the immediate aftermath of the flotation. This Act was required to bring Irish legislation into line with international practice to facilitate price stabilisation on the Irish Stock Exchange.

The shares were offered to the Public in July 1999. Both Government and the Company agreed the prospectus and the price range for the shares of £2.64 to £3.27 that was set prior to the flotation.

The flotation price approved by the Cabinet following the closing date for the receipt of applications for shares was £3.07.

Costs of Flotation

The cost of the flotation was £76.9m which is approximately 2.3% of the £3.3bn raised in the IPO and was funded out of the Vote for Public Enterprise. An amount of £9.2m is due from the Company in respect of their portion of the total cost of the flotation. The provision in the Estimates was originally set at £40m but this had been calculated on the basis that the share holding would have been disposed of in tranches. A Supplementary Estimate of £40m was required to meet the additional costs associated with the sale.

Details of the costs of the flotation are as follows:

	£m
Joint Advisers	58.6
Advertising	3.8
Public Relations	3.4
Printing	3.4
Postal Costs	3.3
Processing of Applications	1.9
Legal	1.5
Other	<u>1.0</u>
Total	<u>76.9</u>

Share Acquisitions and Amounts Paid

The following is a summary of the share acquisitions and the amounts paid

Year	Purchaser	No of Shares Acquired	Amount Paid £	Average Price per share £
1996 - 2000	Comsource	772,739,342	1,520,371,976	1.97
1999 - 2000	ESOP	218,574,842	190,000,000	0.87
1999	ESOP	110,391,334	Nil*	Nil*
1999	IPO	1, 081,490,338**	3,320,175,339	3.07
Total		2,183,195,856***	5,030,547,315	

* These shares were distributed to employees in return for agreed productivity measures which were expected to deliver payroll cost savings of £110m over five years.

** This figure does not include the 23,810,828 shares which have been retained by the Ministers for distribution as a loyalty bonus. 16,047,305 of the bonus shares had been distributed up to 6 September 2000.

*** As at 6 September 2000 the Ministers held 8,583,532 shares, which represented 7,763,523 bonus shares which had not yet been issued or may not be required due to failure of purchasers to hold shares for the required 12 months and 820,009 shares offered for sale in the IPO which had still not been allocated.

Pension Liabilities

The Minister for Finance under the Postal and Telecommunications Services Act, 1983 (as amended) is responsible for meeting and discharging the liability in relation to the pension costs of former staff of the Department of Post and Telegraphs who retired or died before 1 January 1984, and in relation to the costs of pension entitlements, relating to reckonable service prior to 1 January 1984, of staff who transferred to BTE from the Civil Service. Up until April 2000 the Minister provided funds to meet the cost of pensions as they became due for payment. However, at the end of 1999 the Minister paid £800m into a Trust fund which was set up to discharge all his future obligations in relation to the pensions. The Board of Trustees comprises two BTE representatives, four BTE employee representatives and two civil servants. The Exchequer will be liable for any deficit in the event of there being insufficient funds to meet the liabilities. Similarly, in the event of there being surplus funds, such surplus moneys will be surrendered to the Exchequer.